Liwa Holdings Sdn Bhd v Chi Liung Holdings Sdn Bhd & Ors

HIGH COURT (KUALA LUMPUR) — ORIGINATING SUMMONS NO D3-24-198 OF 1993
ARIFIN JAKA J
18 AUGUST 1998

Companies and Corporations *— Debenture — Nature of — Debenture executed by first defendant as security for repayment of loan — Debenture did not give lender power to take over management of first defendant — Whether debenture contravened s 132C of the Companies Act 1965*

Companies and Corporations *— Directors — Authority — Director passed away leaving only one other director — New director appointed — Execution of debenture by board of directors — Whether debenture was executed by someone with the authority and mandate to do so — Whether there was a properly constituted board of directors*

The plaintiff was a majority shareholder in Chi Liung Holdings Sdn Bhd ('Chi Liung'). Chi Liung entered into a loan agreement ('the principal agreement') with the lenders and Amanah Merchant Bank Bhd ('AMBB') as agent whereby the lenders granted to Chi Liung a bridging loan. The principal agreement was amended by a supplemental agreement which provided for the execution of a limited debenture by Chi Liung in favour of AMBB as agent for the lenders as a further security for the repayment of the loan. The plaintiff and Chi Liung executed the supplemental agreement as authorized by their respective board resolutions. In breach of the loan agreement, Chi Liung failed to make repayment as a result of which AMBB, as agent of the lenders, exercised its rights under the debenture and appointed a receiver and manager. The plaintiff filed an application seeking a declaration that the limited debenture entered into between Chi Liung and AMBB was illegal, null and void. It was contended that the letters of administration of the estate of one Dato' Tong Lee Hwa ('Dato' Tong'), one of the shareholders of Chi Liung, was only extracted after the board resolutions were passed. Thus the estate of Dato' Tong could not be represented at any meeting of Chi Liung for the purpose of the creation of the debenture. The plaintiff also asserted that it did not and could not attend any meeting for the creation of the debenture as the late Dato' Tong was also a substantial shareholder of the plaintiff. Under these circumstances, it was contended that the debenture was not lawfully created. The issues before the court were whether: (i) the debenture was executed by someone who had the authority or mandate to do so on behalf of Chi Liung; (ii) the debenture contravened s 132C of the Companies Act 1965 ('the Act'); and (iii) AMBB was bound to enquire into the internal management of Chi Liung.

Held, dismissing the plaintiff's application:

(1) The debenture was created pursuant to the supplementary agreement which was signed by the plaintiff and Chi Liung under their respective board resolutions. A resolution passed at a general meeting of the plaintiff and Chi Liung was not necessary for the purpose of the execution by them of the supplementary agreement. A board resolution for that purpose would be sufficient.

The articles of association of Chi Liung provided that the directors had the power to create the debenture. However, it was evident that on the death of Dato' Tong, there was only one director. It was provided that in such circumstances, the continuing director had the power to appoint a new director to fill the vacancy and one Tong King Kan was appointed. Therefore, there was in existence a properly constituted board of directors and the board resolution passed by Chi Liung was valid. Therefore, the debenture was also valid and enforceable (see pp 470I, 471A, C–I and 472A).

(2) The debenture was not a disposal of Chi Liung's undertaking or property as contemplated under s 132C(1), nor did it give the lender bank power to take over the management Chi Liung. It was nothing more than security for the repayment of the loan by Chi Liung which was a valid form of security within the realm of commercial transactions pertaining to loans granted by financial institutions to their borrowers. In the circumstances, the debenture did not contravene s 132C(1) of the Act and therefore, it was not invalid (see pp 472I and 473A–B); *Che Wan Development Sdn Bhd v Co-operative Central Bank Bhd* [1990] 2 MLJ 365 and *Re Yallamma Cotton & Silk Mills Co Ltd* (1970) 40 Comp Case 466 (Mys) distinguished.

(3) AMBB as the agent of the borrowers was entitled to assume that the debenture was properly created and the signatories to the debenture were duly authorized to do so. The fact that AMBB had knowledge of Dato' Tong's death could not be construed as a notice that the acts of the directors of Chi Liung were not properly performed. Moreover, it was clearly stated that the debenture was issued pursuant to the company's memorandum and articles of association. AMBB was not bound to inquire as to the company's capacity to enter into the debenture or as to any such limitation on the director's powers and the parties were presumed to have acted in good faith unless the contrary was proved. In the instant case, the plaintiff had not adduced evidence to prove that the parties had not acted in good faith (see p 473C–G).

[Bahasa Malaysia summary

Plaintif adalah pemegang saham utama dalam Chi Liung Holdings Sdn Bhd ('Chi Liung'). Chi Liung telah mengikat satu perjanjian

A pinjaman ('perjanjian utama tersebut') dengan pemberi-pemberi pinjaman dan Amanah Merchant Bank Bhd ('AMBB') sebagai ejen di mana pemberi-pemberi pinjaman tersebut telah memberikan satu pinjaman penyambungan kepada Chi Liung. Perjanjian utama tersebut telah dipinda oleh satu perjanjian tambahan yang memperuntukkan bagi penyempurnaan satu debentur terhad oleh Chi Liung atas nama
B AMBB sebagai ejen bagi pemberi-pemberi pinjaman sebagai jaminan selanjutnya untuk pembayaran balik pinjaman tersebut. Plaintif dan Chi Liung telah menyempurnakan perjanjian tambahan tersebut sepertimana yang dibenarkan oleh resolusi lembaga mereka masing-masing. Dalam kemungkiran perjanjian pinjaman tersebut, Chi Liung
C gagal untuk membuat pembayaran balik dan akibatnya AMBB, sebagai ejen pemberi-pemberi pinjaman, telah melaksanakan haknya di bawah debentur tersebut dan telah melantik penerima dan pengurus. Plaintif telah memfailkan satu permohonan untuk mendapatkan perisytiharan bahawa debentur terhad yang telah diikat antara Chi Liung dan AMBB adalah salah di sisi undang-undang, tak sah dan batal. Adalah
D dihujahkan bahawa surat-surat kuasa mentadbir bagi harta pusaka seorang bernama Dato' Tong Lee Hwa ('Dato' Tong'), salah seorang pemegang saham Chi Liung, telah hanya dicabut selepas resolusi lembaga diluluskan. Justeru itu harta pusaka Dato' Tong tidak boleh diwakili di mana-mana mesyuarat Chi Liung bagi tujuan mewujudkan
E debentur tersebut. Plaintif juga menegaskan bahawa ia telah tidak dan tidak boleh menghadiri sebarang mesyuarat bagi kewujudan debentur tersebut kerana mendiang Dato' Tong adalah juga merupakan pemegang saham plaintif yang substansial. Di bawah keadaan ini, telah dihujahkan bahawa debentur tersebut telah tidak diwujudkan secara sah. Isu-isu di hadapan mahkamah adalah sama
F ada: (i) debentur tersebut telah disempurnakan oleh seseorang yang mempunyai kuasa atau mandat untuk melakukan sedemikian bagi pihak Chi Liung; (ii) debentur tersebut melanggari s 132C Akta Syarikat 1965 ('Akta tersebut'); dan (iii) AMBB wajib menyiasat pengurusan dalaman Chi Liung.

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Diputuskan, menolak permohonan plaintif:

(1) Debentur tersebut telah diwujudkan menurut perjanjian tambahan yang telah ditandatangani oleh plaintif dan Chi Liung di bawah resolusi lembaga mereka masing-masing. Satu resolusi yang telah
H diluluskan di mesyuarat am plaintif dan Chi Liung tidak perlu bagi tujuan penyempurnaan oleh mereka akan perjanjian tambahan tersebut. Resolusi lembaga bagi tujuan itu adalah memadai.

Perkara-perkara persatuan Chi Liung memperuntukkan bahawa pengarah-pengarah mempunyai kuasa untuk mewujudkan
I debentur tersebut. Walau bagaimanapun, adalah jelas bahawa ketika kematian Dato' Tong, hanya terdapat seorang pengarah sahaja. Adalah diperuntukkan bahawa dalam keadaan yang sedemikian, pengarah yang berterusan mempunyai kuasa untuk

melantik seorang pengarah baru untuk memenuhi kekosongan dan seorang yang bernama Tong King Kan telah dilantik. Dengan itu, wujudnya lembaga pengarah berperlembagaan yang sempurna dan resolusi lembaga yang diluluskan oleh Chi Liung adalah sah. Dengan itu, debentur tersebut adalah juga sah dan berkuatkuasa (lihat ms 470I, 471A, C–I dan 472A).

(2) Debentur tersebut bukannya satu pelepasan akan akujanji atau hartanah Chi Liung sepertimana yang ditetapkan di bawah s 132C(1), ia juga tidak memberikan kuasa kepada bank pemberi pinjaman untuk mengambil alih pengurusan Chi Liung. Ia adalah semata-mata jaminan untuk pembayaran balik akan pinjaman tersebut oleh Chi Liung yang mana merupakan satu bentuk jaminan yang sah di dalam lingkungan transaksi-transaksi komersil berhubung dengan pinjaman-pinjaman yang diberikan oleh institusi-institusi kewangan kepada peminjam-peminjam mereka. Dalam keadaan tersebut, debentur itu tidak melanggari s 132C(1) Akta tersebut dan dengan itu, ia adalah sah (lihat ms 472I dan 473A–B); *Che Wan Development Sdn Bhd v Co-operative Central Bank Bhd* [1990] 2 MLJ 365 dan *Re Yallamma Cotton & Silk Mills Co Ltd* (1970) 40 Comp Case 466 (Mys) dibeza.

(3) AMBB sebagai ejen peminjam-peminjam tersebut berhak untuk menjangkakan bahawa debentur tersebut telah diwujudkan dengan sempurna dan penandatangan-penandatangan pada debentur tersebut telah diberi kuasa untuk melakukan sedemikian. Hakikat bahawa AMBB mengetahui mengenai kematian Dato' Tong tidak boleh ditafsirkan sebagai satu notis bahawa perbuatan-perbuatan pengarah-pengarah Chi Liung telah tidak dilaksanakan dengan sempurna. Lagipun, ia telah dinyatakan dengan jelas bahawa debentur tersebut telah dikeluarkan menurut memorandum dan perkara-perkara persatuan syarikat tersebut. AMBB tidak terikat untuk menyiasat keupayaan syarikat tersebut untuk mengikat debentur itu atau berhubung dengan mana-mana penghadan ke atas kuasa-kuasa pengarah dan pihak-pihak tersebut dianggapkan telah bertindak dengan suci hati melainkan perkara yang sebaliknya terbukti. Dalam kes ini, plaintif telah tidak mengemukakan keterangan untuk membuktikan bahawa pihak-pihak tersebut telah tidak bertindak dengan suci hati (lihat ms 473C–G).]

Notes

For a case on the nature of debenture, see 3 *Mallal's Digest* (4th Ed, 1997 Reissue) para 71.

For a case on the authority of directors, see 3 *Mallal's Digest* (4th Ed, 1997 Reissue) paras 103–110.

Cases referred to

ANZ Banking Group Ltd v Australian Glass and Mirrors Pty Ltd & Anor (1991) 9 ACLC 702 (refd)

Che Wan Development Sdn Bhd v Co-operative Central Bank Bhd [1990] 2 MLJ 365 (distd)
Public Bank Bhd v Metro Construction Sdn Bhd [1991] 3 MLJ 56 (refd)
Yallamma Cotton & Silk Mills Co Ltd, Re (1970) 40 Comp Case 466 (Mys) (distd)

Legislation referred to

Companies Act 1965 ss 122(1), 132C, 186(1)

Mary Sitravelu (*RV Lingam & Co*) for the plaintiff.
GT Rajan (*GT Rajan & Co*) for the first defendant.
J Pillay (*Louis Ting* with him) (*Kadir Tan & Ramli*) for the second defendant.
SY Ng (*Raja Darryl & Loh*) for the third defendant.

Arifin Jaka J: On 18 October 1993, Liwa Holdings Sdn Bhd ('the plaintiff') filed this originating summons against the first defendant, Chi Liung Holdings Sdn Bhd ('Chi Liung') and the second defendant, Amanah Merchant Bank Bhd ('AMBB') seeking a declaration that the limited debenture entered into between Chi Liung and AMBB on 17 August 1989, registration No 21607/89 ('the debenture') is illegal, null and void and unenforceable and is oppressive and in total disregard to the interest of plaintiff. Pursuant to an order of court dated 23 June 1995, Lim Tian Huat, the receiver and manager of Chi Liung who was appointed under the terms of the debenture, was added as the third defendant.

The brief facts are that the plaintiff was at the material time a majority shareholder holding 27,397,000 shares out of the issued and paid up shares of 37,670,000 in Chi Liung. On 23 September 1985, Chi Liung entered into a loan agreement ('the principal agreement') with a syndicate of financial institutions named in Appendix A therein as lenders and AMBB as manager and Malaysia Borneo Finance Corp (M) Bhd as co-manager and AMBB as agent whereby the lenders granted to Chi Liung a bridging loan ('the facility') in the maximum aggregate amount of Ringgit Malaysia forty six million (RM46,000,000) only. The principal agreement was amended by a supplemental agreement dated 20 July 1987 and by a further supplemental agreement dated 17 August 1989. The further supplemental agreement provides, inter alia, for the execution of a limited debenture by Chi Liung in favour of AMBB as agent for the lenders as a further security for the repayment of the facility, interest and other moneys convenanted in the principal agreement to be paid by Chi Liung to the lenders. Pursuant to the further supplemental agreement, Chi Liung executed the debenture on 17 August 1989 in favour of AMBB as trustee and agent of the lenders.

The facility was utilized by Chi Liung. In breach of the loan agreement, Chi Liung had failed to make repayment as a result of which AMBB as agent of the lenders exercised its rights under the debenture and appointed Lim Tian Huat, the third defendant herein, as a receiver and manager of all the properties, assets and undertaking of Chi Liung. The appointment

was made on 29 December 1992 and notice of the appointment was filed with the Registrar of Companies in compliance with s 186(1) of the Companies Act 1965 ('the Act'). About ten months after the appointment of the receiver and manager, the plaintiff formed the opinion and contended that the debenture was illegal, null and void and unenforceable and only then it registered its objection by filing the instant application.

In deciding whether the debenture is illegal, null and void, the court has to consider the following questions:

(a) whether the debenture was executed by someone who had authority or mandate to do so on behalf of Chi Liung;

(b) whether the debenture contravenes s 132C of the Act; and

(c) whether AMBB (the second defendant) is bound to enquire into the internal management of Chi Liung.

I shall now proceed to consider these questions. To begin with, it is to be noted that it is not disputed by the parties that the debenture was executed on 25 July 1989. As regards the first question, namely whether the director who executed the debenture was authorized to do so, it is necessary to examine the circumstances which led to the creation of the debenture. The debenture was issued pursuant to Chi Liung's memorandum and article of association. It was created under the terms of the further supplemental agreement dated 17 August 1989 which was entered into by the plaintiff and Chi Liung as parties thereto. The plaintiff executed the supplemental agreement as authorized by its board resolution passed on 25 July 1989 (exh LTH8 in encl 10) which provided, inter alia, that the plaintiff do enter into a supplemental agreement amending the principal agreement and the security documents upon the terms and conditions of the draft supplemental agreement dated 29 June 1989 which was produced at the board meeting. Chi Liung also executed the supplemental agreement under the authorization of its board resolution dated 25 July 1989 (exh LTH7 in encl 10). It is important to note that both the resolutions gave Chong Mooi Lan and the secretaries of the plaintiff and Chi Liung to assent to all amendments to the draft supplemental agreement and the draft documents as the lenders may require.

It was contended by learned counsel of the plaintiff that the letters of administration of the estate of Dato' Tong Lee Hwa who died on 31 December 1988 was only extracted on 9 December 1992. The estate of Dato' Tong Lee Hwa who was one of the shareholders of Chi Liung could not be represented at any meeting of Chi Liung for the purpose of the creation of the debenture. The plaintiff also asserted that it did not and could not attend any meeting for the creation of the debenture as the late Dato' Tong Lee Hwa was also a substantial shareholders of the plaintiff. Under these circumstances, it was contended that the debenture was not lawfully created. With the greatest respect, I do not agree with the contentions of learned counsel. It cannot be denied as I had said earlier that the debenture was created pursuant to the further supplementary agreement which was signed by the plaintiff and Chi Liung under their respective board resolutions. A resolution passed at a general meeting of

A the plaintiff and Chi Liung is not necessary for the purpose of the execution by them of the supplementary agreement. A board resolution for that purpose would be sufficient as in this case. It is not now open for the plaintiff to say that its board resolution was not proper.

The next related point raised by the plaintiff alleges that the debenture B was executed without the shareholders resolution of Chi Liung. The question that must be answered to satisfy this point is whether a shareholders resolution was required for the purpose of the execution of the debenture. Under art 55 of the articles of association of Chi Liung, the directors may raise or secure the repayment of such sum or sums in such manner and upon such terms and conditions in all respects as they think fit and, in C particular, by issue of bonds, perpetual or redeemable debentures or debenture stock or any mortgage, charge or other security. It is clear therefore that the directors have the power to create the debenture under a resolution passed by the board. In this respect, the question that arises is whether there existed a properly constituted board of directors of Chi D Liung after the death of Dato' Tong that could lawfully pass the resolution dated 25 July 1989 that authorized the execution of the debenture.

Under s 122(1) of the Act, it is stated that every company shall have at least two directors and this is enshrined in art 86 of Chi Liung's articles of association which states 'Unless otherwise determined by a general meeting, the number of directors shall not be less than two or more E than five'.

It is in evidence that on the death of Dato' Tong Lee Hwa on 31 December 1988, the only director left is Chong Mooi Lan and on 9 January 1989, another director, Tong King Kan, was appointed (see exh KTR4 — encl 12).

F Learned counsel for AMBB (the second defendant) contended that under art 88 of Chi Liung's articles of association, there is an implicit power for the remaining director to appoint an additional director to fill a vacancy. The relevant article in my view is art 92 where it is provided, inter alia, to the effect that the continuing directors shall not act, except in G emergencies or for the purpose of filling up vacancies, so long as the number is below the minimum. It is therefore clearly provided that in the instant case Chong Mooi Lan, the continuing director, had the power to appoint a new director in the person of Tong King Kan to fill a vacancy. It follows therefore after the death of Dato' Tong Lee Hwa there was in existence a properly constituted board of directors. The board resolution H passed on 25 July 1989 by Chi Liung was valid. The resolution authorized Chi Liung to issue the debenture and that the common seal of Chi Liung be affixed in accordance with its articles of association. Article 118 which was amended by an extraordinary general meeting held on 10 February 1982 and duly filed with the Registrar of Companies I on 11 February 1982 provides that: 'every instrument to which the seal is affixed shall be signed ... by Datin Chong Mooi Lan, director and countersigned by the secretary ... .' The debenture was signed by Chong Mooi Lan and countersigned by the secretary on behalf of Chi Liung as authorized by art 118. It therefore follows that the debenture was executed

by the director who had authority and mandate to do so. The allegation advanced by the plaintiff that the debenture is illegal, null and void is not sustainable and for this reason, I hold that the debenture is valid and enforceable.

Another question posed by the plaintiff and Chi Liung (first defendant) is the debenture contravenes s 132C(1) of the Act. This section provides, inter alia, that notwithstanding anything in a company's memorandum or articles, the directors shall not carry into effect any proposal or execute any transaction for the disposal of a substantial portion of the company's undertaking or property, which would materially and adversely affect the performance or financial position of the company, unless the proposal or transaction has been approved by the company in general meeting. Learned counsel for the plaintiff adopted the argument of learned counsel for Chi Liung (first defendant) by saying that the debenture contravenes s 132C(1). Learned counsel for Chi Liung submitted that the debenture which serves as a security for the loan taken by Chi Liung by way of charging all its assets and undertaking without the shareholders resolution is prohibited in law. In support of this proposition, learned counsel relied on the case of *Che Wan Development Sdn Bhd v Co-operative Central Bank Bhd* [1990] 2 MLJ 365. With respect, this case dealt with s 133 of the Act, and has no relevance to the question posed in the instant case which concerns s 132C. This case does not help the plaintiff and Chi Liung at all.

Learned counsel also relied on the case of *Re Yallamma Cotton & Silk Mills Co Ltd* (1970) 40 Comp Case 466 (Mys) and contended that the debenture was invalid as it permits the lenders to take over the management of the business of Chi Liung. In this case, there was a clause in the debenture which created the floating charge empowering the lender bank to actually take over the management of the business of the borrower company. This clause was held to be invalid because to permit the bank to take over the management of the company's business itself may be regarded as a disposal by the company of the whole of its undertaking to the bank. This case is not applicable to the instant case as there is no such clause giving such power to the lenders. The power is given to the receiver and manager who was an agent of the borrower. Even assuming that there is such a clause in the debenture in the instant case empowering the lenders to take over the management of the company's business, the invalidity of the clause need not be said to have a fatal effect on the entire transaction itself. This clause alone could be struck down to the extent it empowered the taking over of the management of the business of the company without affecting the validity of the enforceability of the rest of the terms (*Re Yallamma*'s case). For this reason, I hold that the contention of Chi Liung on this point has no merits whatsoever.

The question that arises in the instant case is whether the debenture has the effect of a disposal of the company's undertaking or property which would materially and adversely affect the performance or financial position of the company as envisaged in s 132C. It is my considered opinion that the debenture is not a disposal of Chi Liung's undertaking or property as contemplated under s 132C(1). It is nothing more than a security for the

repayment of the loan by Chi Liung which is a valid form of security within the realm of commercial transaction pertaining to loans granted by financial institutions to their borrowers. In the circumstances, I rule that the debenture does not contravene s 132C(1) of the Act and it follows that it is not invalid.

The last point to be decided is whether the legendary rule in *Turquand*'s case applies in this case. The rule protects a third party dealing with the company in good faith who is entitled to assume that acts within the company's memorandum and articles of association have been properly performed and is not bound to inquire as to their regularity.

In the instant case, AMBB, as the agent of the borrowers, is entitled to assume that the debenture was properly created and the signatories to the debenture were duly authorized to do so. The documents filed by Chi Liung with the Registrar of Companies clearly show that the directors of Chi Liung were lawfully appointed and that they were authorized to pass a resolution to issue the debenture. Learned counsel for AMBB referred to *ANZ Banking Group Ltd v Australian Glass and Mirrors Pty Ltd & Anor* (1991) 9 ACLC 702 where it was held that from the description of the persons in the returns submitted to Registrar of Companies, it was reasonable to assume that the persons in the returns had been appointed as directors of the company and hence was authorized to transact on behalf of the company notwithstanding that changes has taken place within the knowledge of the company. The fact that AMBB had knowledge of Dato' Tong Lee Hwa's death cannot be construed to be a notice that the acts of the directors of Chi Liung were not properly performed. AMBB is therefore not deprived of the benefit of the rule in *Turquand*'s case in their favour. This is because the death of Dato' Tong is a separate issue and is not relevant for the purpose of the debenture under the company's separate identity doctrine.

It is clearly stated that the debenture is issued pursuant to the company's memorandum and articles of association. AMBB is not bound to inquire as to the company's capacity to enter into it or as to any such limitation on the director's powers and the parties will be presumed to have acted in good faith unless the contrary is proved (see *Public Bank Bhd v Metro Construction Sdn Bhd* [1991] 3 MLJ 56). In the instant case, the plaintiff had not adduced evidence to prove that the parties have not acted in good faith.

On careful consideration of the submission of counsel for all the parties and on the evidence available and in the circumstances of the case, I am convinced that the debenture was not invalid, null and void. Accordingly, the plaintiff's application is dismissed with costs.

Plaintiff's application dismissed.

Reported by Jafisah Jaafar